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# In the Supreme Court of the United States

OCTOBER TERM, 1994

ROBERT L. DUFRESNE, CAROLYN S. DUFRESNE, JERRY R. DIXON, PATRICIA A. DIXON, RICHARD HONGSERMEIER, FIORELIA HONGSERMEIER, HOYT W. YOUNG, BARBARA D. YOUNG, TERRY D. OWENS, AND GLORIA OWENS, PETITIONERS

*v.*

COMMISSIONER OF INTERNAL REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT*

## BRIEF FOR THE RESPONDENT IN OPPOSITION

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11 pp

## QUESTION PRESENTED

Whether the court of appeals erred in directing the Tax Court to determine on remand whether the decisions in these cases should be voided due to the misconduct of trial counsel.

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### OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-7a) is reported at 26 F.3d 105. The opinion of the Tax Court (Pet. App. 10a-188a) is reported at 62 T.C.M. (CCH) 1440.

### JURISDICTION

The judgment of the court of appeals was entered on June 14, 1994. A petition for rehearing was denied on October 25, 1994. (Pet. App. 8a-9a). The petition for a writ of certiorari was filed on January 23, 1995. The

jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

## STATEMENT

1. Henry Kersting created and administered assorted "investment programs" that he sold primarily to commercial airline pilots. Each of the programs followed the same basic pattern. In each program, a client obtained a primary loan from one Kersting corporation in order to purchase stock or an investment certificate in another Kersting corporation. The client simultaneously obtained a "leverage" loan from another Kersting corporation in an amount equal to one year's interest on the primary loan, the proceeds of which were used to pay interest on the primary loan. Thereafter, the corporation in which the client had purchased stock purported to made a nontaxable distribution in an amount equal to the amount of the "leverage" loan, the proceeds of which were applied to repay that loan. At the end of the year, if the transactions were not repeated, the taxpayer returned the stock or investment certificate to the Kersting corporation in satisfaction of the primary loan. The "interest" purportedly paid was claimed as a deduction by the client on his tax return (Pet. App. 4a, 34a-58a).

The Commissioner disallowed the interest deductions claimed by the taxpayers who participated in the Kersting programs. Approximately 1,300 petitions were filed in the Tax Court by participants in the programs seeking redeterminations of the deficiencies in income tax determined by the Commissioner. From those cases, by agreement of the parties, 14 cases were chosen as test

cases and were consolidated for trial and opinion.[1] Parties in most of the non-test cases stipulated to be bound by the outcome of the test cases (Pet. App. 5a, 13a).

After trial of the test cases, the Tax Court found that the interest deductions claimed by the taxpayers were not allowable. The court concluded that the Kersting plans were shams and that the purported loans did not create genuine indebtedness. On March 13, 1992, the Tax Court entered decisions against each of the test case petitioners determining deficiencies in their tax liabilities in accordance with its opinion (Pet. App. 5a).

On June 9, 1992, the Commissioner filed motions in three of the test cases—*Thompson*, *Cravens*, and *Rina*—to vacate the decisions entered in those cases. In her motions, the Commissioner stated that information she had recently obtained indicated that a settlement agreement had been entered into between her district counsel and Mr. Thompson prior to trial that was contingent upon Mr. Thompson not prevailing. The Commissioner advised the court that the contingent settlement agreement had not been divulged to the Commissioner's Regional or National offices, to other taxpayers or their counsel or to the court itself. The motions stated further that a contingent settlement might also have been reached with Mr. Cravens prior to trial which similarly had not been disclosed. The Commissioner requested the Tax Court to hold a hearing to determine the effect, if any, that such agreements might have had on the trial and on the court's opinion in the test cases (Pet. App. 5a, 197a-214a). In subsequent filings, the Commissioner stated that the

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[1] The test cases were those filed by the Dixons, the DuFresnes, the Youngs, the Owenses, the Hongsermeiers, Mr. Rina, the Thompsons, and the Cravenses.

contingent agreement in the *Thompson* cases was based on an agreement to reduce the amount of Mr. Thompson's deficiencies in tax in order to generate a tax refund that would be used to pay the Thompsons' legal fees (Pet. App. 6a).

On June 22, 1992, the Tax Court entered an order finding, in a case in which the petitioner had not entered into a settlement agreement, that the failure to disclose the contingent settlement agreements with Thompson and Cravens was harmless. The court denied the Commissioner's motion to vacate the decision entered in that case, stating as follows (Pet. App. 215a-216a):

> The Court has reviewed the testimony of Cravens, the testimony of Thompson, the stipulated facts and the stipulated exhibits relating to the Cravenses and the Thompsons, and the exhibits offered through Thompson as a witness. The Court finds that these reviewed items had no material effect on the opinion which the Court filed on December 11, 1991, as that opinion relates to petitioner Rina. If the reviewed items were stricken from the record, the Court would file an opinion in all material respects like the opinion it filed on December 11, 1991 (with the exception of certain portions relating specifically and expressly to the Cravenses or the Thompsons), and the Court's findings, analyses, and conclusions relating to petitioner Rina would remain the same. No purpose would be served by having a hearing on the matter.

Over the objection of the Commissioner, the Tax Court then entered new decisions in the *Thompson* cases giving the Thompsons the benefit of the settlements to which the Commissioner's district counsel had agreed. The court entered stipulated decisions in the *Cravens*

cases giving the Cravenses the benefit of settlements agreed to in their cases.

2. The court of appeals vacated the decisions entered in petitioners' cases and remanded the cases to the Tax Court. The court of appeals noted that the Tax Court had not conducted a hearing before determining whether government trial counsel's failure to disclose the contingent settlements was harmless. The court concluded that it could not determine from the record "whether the extent of misconduct rises to the level of a structural defect voiding the judgment as fundamentally unfair, or whether, despite the govern-ment's misconduct, the judgment can be upheld as harmless error" (Pet. App. 6a). The court of appeals directed the Tax Court to conduct an evidentiary hearing on remand and "to determine the full extent of the admitted wrong done by the government trial lawyers" (Pet. App. 6a-7a).

## DISCUSSION

The court of appeals vacated the adverse decisions entered against petitioners by the Tax Court and remanded the cases for further fact-finding. Review of the interlocutory decision of the court of appeals is not warranted at this time. *Brotherhood of Locomotive Firemen & Enginemen* v. *Bangor & Aroostook R.R.*, 389 U.S. 327, 328 (1967); *Hamilton-Brown Shoe Co.* v. *Wolf Brothers & Co.*, 240 U.S. 251, 258 (1916); *Virginia Military Institute* v. *United States*, 113 S. Ct. 2431, 2432 (1993) (Scalia, J.). Petitioners may prevail before the Tax Court on remand. Once the Tax Court has conducted the evidentiary hearing mandated by the court of appeals, made appropriate findings and legal conclusions, and entered final decisions in petitioners' cases, petitioners may in any event appeal those decisions to the Ninth Circuit if appropriate and then seek further

review by this Court if needed. Review at this time of the interlocutory order remanding the case for further findings would be premature.

Moreover, the judgment directing the Tax Court to determine after a hearing whether the misconduct of the government's trial attorneys rose to the level of a structural defect or was harmless is consistent with established law. *Arizona* v. *Fulminante*, 499 U.S. 279, 309-310 (1991); see Tax Ct. R. 160; Fed. R. Civ. P. 61. Petitioners contend (Pet. 5-6) that the inclusion of their cases among the test cases to be tried on their merits created an implied contract with the government that was breached by the conduct of the government's trial counsel.[2] Although the conduct of the government's trial counsel may have adversely affected petitioners' procedural rights to a fair trial, there was no implied contract between petitioners and the government. The court of appeals recognized that petitioners may not have received a fair trial and, for that reason, it vacated the adverse decisions entered against petitioners by the Tax Court and remanded the cases to the Tax Court for further proceedings. There is no special justification warranting review by this Court of that interlocutory order at this time.

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[2] Contrary to petitioners' contention (Pet. 8), they are not parties to the stipulations to be bound by the outcome of the test cases that were made by non-test case taxpayers. Petitioners did not execute the stipulations that were entered into with the non-test case taxpayers, nor were those stipulations entered into for petitioners' benefit. Instead, petitioners' cases were among those chosen by agreement of the parties to be tried in the Tax Court and decided on their merits. The stipulations entered into by the non-test case taxpayers therefore have no relevance to petitioners' cases.

## CONCLUSION

The petition for a writ of certiorari should be denied.
Respectfully submitted.

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